

SECURED TRANSACTIONS: SALES OF ACCOUNTS, CONTRACT RIGHTS, AND CHATTEL PAPER

LAWRENCE J. BURNS*

INTRODUCTION AND DEFINITIONS

On May 18, 1961, Senate Bill No. 5 of the 104th General Assembly was signed by the Governor of Ohio, and the Uniform Commercial Code became law to take effect on July 1, 1962.

Article 9, dealing with secured transactions and sales of accounts, contract rights, and chattel paper, is by far the most complex and far reaching of the nine substantive articles contained in the "Code." The provisions of this article are found in Ohio Revised Code sections 1309.01 to 1309.50, inclusive.

This paper will not attempt a detailed comparison of article 9 with existing Ohio statutes or cases. An attempt will be made simply to explain the new law and methods of securing an interest in personal property on and after July 1, 1962. For a detailed comparison of existing Ohio law to the provisions of the Uniform Commercial Code the reader is referred to Ohio Legislative Service Commission Bulletin No. 1958-1 entitled "Ohio Annotations to Uniform Commercial Code." Similar comparisons to the provisions of article 9 are contained in previous issues of the Ohio State Law Journal.¹

The goal of article 9 is to:

provide a simple and unified structure within which the immense variety of present day secured financing transactions can go forward with less costs and with greater certainty.²

No one has taken issue with this stated aim. A great deal of controversy, however, arose as to some of the provisions of article 9 by which this goal was to be achieved.

Article 9 does not seek to amend existing statutes relating to secured financing of personal property but to repeal them. Existing statutes in this field were not adopted as part of a comprehensive plan to meet commercial financing needs as they exist today but, rather, were adopted piecemeal over a long span of years as the need for new financing devices presented themselves. The result has been the growth of a number of different devices, each with its own set of formal requirements and rules regulating the rights of the parties in relation to each other and to third persons.

* Of the firm of Nappi, Cunningham & Burns, Columbus, Ohio; Legislative Council for Ohio Bankers Association.

¹ 14 Ohio St. L. J. 1-93 (1953); 15 Ohio St. L. J. 1-75 (1954).

² Comment, UCC §§ 9-101.

Article 9, on the other hand, is a comprehensive approach to present day financing needs. It recognizes that all of our existing security devices were designed for one purpose; to give certain creditors exclusive rights in particular property out of which their claims might be satisfied in the event of insolvency. This interest in property is described as a "security interest." The security interest is the sole "lien" given under article 9 regardless of the type of collateral involved or the number of different types of collateral. The method of obtaining the security interest generally consists of two steps; creation and attachment of the security interest and perfection of the security interest.

The reader may have noticed several unfamiliar terms in the preceding paragraph. In keeping with the approach of creating a new system of secured financing of personal property, the drafters of article 9 deliberately developed completely new terminology having no "common law or statutory roots."³

Many familiar terms have been ascribed new meanings. Gone from usage in so far as they apply to personal property are such terms as "chattel mortgage," "conditional sale," "factor's lien," "mortgagor" and "mortgagee." A few of the most often used of these new terms should be defined before undertaking a study of the detailed provisions of article 9. A security interest is defined as follows:⁴

Sec. 1301.01.(KK) "Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer, section 1302.42 of the Revised Code, is limited in effect to a reservation of a "security interest." The term also includes any interest of a buyer of accounts, chattel paper, or contract rights which is subject to sections 1309.01 to 1309.50, inclusive, of the Revised Code. The special property interest of a buyer of goods on identification of such goods to a contract for sale under section 1302.42 of the Revised Code is not a "security interest," but a buyer may also acquire a "security interest" by complying with sections 1309.01 to 1309.50, inclusive, of the Revised Code. Unless a lease or consignment is intended as security, reservation of the title thereunder is not a "security interest" but a consignment is in any event subject to the provisions on consignment sales, section 1302.39 of the Revised Code. Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make lease one intended for security, and (b) an agreement that upon

³ Comment, UCC §§ 9-101.

⁴ Ohio Rev. Code § 1301.01 (KK).

compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

The terms "debtor" and "secured party" are defined in Revised Code section 1309.01:

(A)(4) "Debtor" means the person who owes payment or other performance of the obligation secured, whether or not he owns or has rights in collateral, and includes the seller of accounts, contract rights, or chattel paper. Where the debtor and the owner of the collateral are not the same person, the term "debtor" means the owner of the collateral in any provision of sections 1309.01 to 1309.50, inclusive of the Revised Code dealing with the collateral, the obligator in any provision dealing with the obligation, and may include both where the context so requires;

(A)(9) "Secured party" means a lender, seller, or other person in whose favor there is a security interest, including a person to whom accounts, contract rights, or chattel paper have been sold. . . .

The phrase "security agreement" means, "an agreement which creates or provides for a security interest."⁵

A "purchase money security interest" is defined in Revised Code section 1309.05 as a security interest that is:

(A) taken or retained by the seller of the collateral to secure all of (or) part of its price; or

(B) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

The terms "attach" and "perfect" are not defined as such. It is enough here that we understand that before the secured party can have a security interest enforceable against the debtor his interest must "attach" to the collateral. Before he can have a security interest enforceable against third persons he must "perfect" his security interest.

To best understand the changes brought about by article 9, a brief review of secured financing as it exists in Ohio today is in order.

SECURITY INTERESTS IN PERSONAL PROPERTY UNDER PRE-CODE OHIO LAW

There are at least seven existing statutory devices for obtaining a security interest in personal property in Ohio today. In addition there are at least four common law devices for obtaining such a security interest.

⁵ Ohio Rev. Code § 1309.02(A)(8).

The statutory devices are "chattel mortgages,"⁶ "conditional sales,"⁷ "factor's liens,"⁸ "assignment of accounts receivable,"⁹ "trust receipts,"¹⁰ "crop mortgages,"¹¹ and "railroad equipment mortgages."¹² All of the sections of law pertaining to the statutory devices will be repealed except those pertaining to railroad equipment mortgages.

The common law devices are the "pledge," "field warehouse," "bailment lease," and "consignment."

Chattel Mortgage

A chattel mortgage is ordinarily a transfer of title to personal property as security for a debt with possession retained by the debtor. Filing is with the county recorder in the county of the debtor's residence, or if a non-resident, with the recorder of the county in which the collateral is located.

Conditional Sale

A conditional sale is a sale upon credit in which the seller reserves title to the goods sold as security for payment of the purchase price. The formal requirements are simple and recording is with the recorder of the county in which the buyer resides, or if a non-resident, with the recorder of the county in which the property is situated.

Factor's Lien

The statutory factor's lien is an arrangement granting the factor a lien upon merchandise owned by the borrower. It usually consists of a written agreement and separate written statements executed by the borrower and delivered to the factor identifying the merchandise subject to the lien. A public notice of the agreement must be filed in the county in which the borrower's principal place of business is located within fifteen days after execution of the agreement.

Assignment of Accounts Receivable

Accounts receivable may be assigned as collateral. The assignment must be in writing, for value, and made contemporaneously with or subsequent to the filing of a notice of assignment, and the assignee is protected only during the effective period of the notice. The notice is filed in the county recorder's office in the county of the assignor's

⁶ Ohio Rev. Code §§ 1319.01-.05, 1319.08-.10 (1953).

⁷ Ohio Rev. Code §§ 1319.11-.19 (1953).

⁸ Ohio Rev. Code §§ 1311.59-.64 (1953).

⁹ Ohio Rev. Code §§ 1325.01-.08 (1953).

¹⁰ Ohio Rev. Code §§ 1316.01-1316.31 (1957).

¹¹ Ohio Rev. Code §§ 1319.09, 1319.10 (1953).

¹² Ohio Rev. Code § 1701.82 (1953).

chief place of business or, if a non-resident, in the county where he maintains his ledger sheet for the particular account.

Trust Receipts

Under this form of security device the debtor is called the "trustee" and the secured party is labeled the "entrustee." Possession of the collateral is in the trustee. The arrangement is created by execution of a written agreement termed a "trust receipt" and filing of a notice that such financing arrangement exists. Such notice is filed with the county recorder of the county where the trustee's chief place of business is located. Trust receipts are used in dealer financing.

Crop Mortgages

The title of this device is self-explanatory. It is a statutory method by which farmers can make a valid mortgage on crops either planted or to be planted within one year from the date of the execution of such mortgage or any extension thereof. It involves simply the execution of a note and chattel mortgage upon such crops. The mortgage is filed with the county recorder of the county in which the crops are to be grown.

Railroad Equipment Mortgages

Again the title is self-explanatory and as no change is made in this device a detailed discussion of the same is not in order.

Pledge

This is the common law device of possession of the collateral as security for the obligation.

Field Warehouse

The field warehouse is a method of maintaining a lien on a constantly changing inventory by establishing a fictional warehouse on the borrower's premises. The field warehouse company operating the warehouse is in possession of the goods and issues for them a warehouse receipt which can be used as collateral for a loan. Goods are released from the warehouse only against payment and additional loans are granted to pay for goods deposited in the warehouse.

Bailment Lease

The bailment lease is simply a chattel lease containing an option to purchase.

Consignment

This is an arrangement whereby a retailer is furnished with an inventory by a wholesaler or manufacturer. Title to the inventory

remains in the wholesaler or manufacturer and the retailer purchases as he makes each retail sale.

SCOPE OF THE CODE

Article 9 applies to any transaction intended to create a security interest in tangible or intangible personal property or fixtures located within this state and to "any sale of accounts, contract rights, or chattel paper."¹³

EXCLUSIONS

Revised Code section 1309.04 sets forth the transactions to which article 9 does not apply. This section states:

Sections 1309.01 to 1309.50, inclusive, of the Revised Code do not apply:

(A) to a security interest subject to any statute of the United States such as the Ship Mortgage Act, 1920, to the extent that such statute governs the rights of parties to and third parties affected by transactions in particular types of property; or

(B) to a lien given by state or other rule of law for services or materials except as provided in section 1309.29 of the Revised Code on priority of such liens; or

(C) to a transfer of a claim for wages, salary, or other compensation of an employee; or

(D) to an equipment trust covering railway rolling stock; or

(E) to a sale of accounts, contract rights, or chattel paper as part of a sale of the business out of which they arose, or an assignment of accounts, contract rights, or chattel paper which is for the purpose of collection only, or a transfer of a contract right to an assignee who is also to do the performance under the contract; or

(F) to a transfer of an interest or claim in or under any policy of insurance; or

(G) to a right represented by a judgment; or

(H) to any right of set-off; or

(I) except to the extent that provision is made for fixtures in section 1309.32 of the Revised Code, to the creation or transfer of an interest in or lien on real estate, including a lease or rents thereunder; or

(J) to a transfer in whole or in part of any of the following: any claim arising out of a tort; any deposit, savings, passbook, or like account maintained with a bank, savings and loan association, credit union, or like organization.

CONFLICTS OF LAW RULES

In this modern age of commercial transactions it is not uncommon for transactions to involve property situated or used in more than one state. Article 9 lays down rules to govern these situations.

¹³ Ohio Rev. Code § 1309.02.

When the collateral is accounts or contract rights, the law of the state where the assignor of the collateral keeps his records concerning them governs the validity of and perfection of a security interest therein.¹⁴ This rule is in general accord with present Revised Code section 1325.02 which makes jurisdiction dependent upon the location of the assignor's ledger sheets.

If the collateral is general intangibles or goods of a type normally used in more than one jurisdiction, the law of the jurisdiction where the chief place of business of the debtor is located governs the validity and perfection of a security interest.¹⁵ This rule would probably alter the present general rule making the validity and effect of the security interest depend on the situs of the collateral.¹⁶

Property already subject to a security interest when it is brought into this state is also covered by article 9. The law of the state where the security interest attached governs unless the parties understood that the property would be kept in this state and it was in fact brought into Ohio within thirty days after the security interest attached. In that event, the laws of Ohio would apply.¹⁷

A perfected security interest in property brought into this state continues perfected in this state for four months with nothing further being done. If perfected in this state within the four month period, perfection continues uninterrupted.¹⁸

CREATING THE SECURITY INTEREST AND ATTACHMENT

The first step in creating a security interest is the agreement. All security interests are either possessory or non-possessory. In non-possessory arrangements the agreement must be in writing.¹⁹

In order to create an interest in the collateral which is enforceable against the debtor, the security interest must attach to the collateral. Under Revised Code section 1309.15 the security interest attaches when there is agreement, value is given and the debtor has rights in the collateral.

The "Code" does not state at what point the debtor may be considered to have rights in the collateral but rather adopts the negative approach. The debtor has no rights in crops till planted, "fish until caught," "in a contract right until the contract has been made," or "in an account until it comes into existence."²⁰

¹⁴ Ohio Rev. Code § 1309.03(A).

¹⁵ Ohio Rev. Code § 1309.03(B).

¹⁶ 9 O. Jur. 2d, Conflicts of Law § 90.

¹⁷ Ohio Rev. Code § 1309.03(C).

¹⁸ Ohio Rev. Code § 1309.03(C).

¹⁹ Ohio Rev. Code § 1309.14.

²⁰ Ohio Rev. Code § 1309.15.

Perfection cannot occur until the security interest has attached.²¹ However, with respect to certain types of collateral, perfection may be accomplished by attachment alone.

Drafting the Security Agreement

One of the most important steps in creation of the security interest is that of drafting the security agreement.

The statutory requirements for a security agreement are few. As mentioned, when perfection is not by possession, the agreement must be in writing.

It must be signed by the debtor and contain a description of the collateral. It must also describe real estate when the collateral is crops, oil, gas or minerals to be extracted or timber to be cut. These are the only mandatory code requirements.²² To make things even less complicated Revised Code section 1309.08 states:

any description of personal property or real estate is sufficient whether or not it is specific if it reasonably identifies what is described.

At first one would think that one simple security agreement containing the above information would suffice, but this is not deemed desirable. There are many optional provisions which should be included in a security agreement. The inclusion or exclusion of various of these provisions again depends upon the type of collateral involved. These optional provisions may be grouped generally into those that determine use and filing requirements and those that deal with the rights and duties of the parties.

The place of filing or necessity, therefore, is determined by the classification into which the collateral falls.²³ As the classification, with respect to goods, depends upon the primary use, this fact must be determined. The secured party must rely upon the debtor for information as to the intended use. This information could be recorded upon a separate financial history form but this would only mean an additional form to be maintained.

The security agreement should contain a warranty as to the intended primary use of the collateral.

The place of filing may depend upon the place where the assignor of accounts receivable keeps his records concerning them.²⁴ In the event the collateral is a movable which may be used in more than one

²¹ Ohio Rev. Code § 1309.22.

²² Ohio Rev. Code § 1309.14.

²³ Ohio Rev. Code § 1309.38.

²⁴ Ohio Rev. Code § 1309.03.

jurisdiction, the secured party must know the location of the debtor's chief place of business.²⁵

As no filing is required to perfect a purchase money security interest in consumer goods or in farm equipment having an original purchase price of \$500.00 or less, the security agreement should reflect whether or not a purchase money security interest is being granted.²⁶

None of the above information is necessary when granting a security interest upon an automobile for article 9 has not altered the method of perfecting a security interest upon motor vehicles. The interest must still be noted upon the certificate of title.²⁷

Some of this information is applicable to one or more types of collateral but not to others. A possible solution would be to prepare a separate form of security agreement for each type of collateral. This would seem unnecessary. A security agreement can be drafted covering a combination of collateral.

It is felt that one security agreement can cover consumer goods, equipment, and farm equipment. Automobiles may also be included under this form but most of the provisions would be superfluous. A separate agreement should be drafted for farm products, for inventory, for accounts receivable, and for documentary collateral.

The second group of covenants which should be contained relate to the rights and duties of the parties. These pertain to insurance, taxes, and rights and duties upon default.

Article 9 permits the obligation to be secured by after acquired property and permits future advances to be included in the original obligation.²⁸ If this coverage is desired, provision must be made in the security agreement.

Article 9 provides that a buyer in the ordinary course of business takes free of a security interest created by his seller even though such interest is perfected and the buyer knows that the security interest exists.²⁹ This rule does not apply to the purchaser of farm products. It does apply, however, to inventory.

The collateral may be removed from the secured parties lien by a sale to a buyer in the ordinary course of business. Article 9 allows the secured party a security interest in the proceeds of the sale of the collateral.³⁰ If this protection is desired, it should also be covered in the security agreement.

²⁵ Ohio Rev. Code § 1309.03.

²⁶ Ohio Rev. Code §§ 1309.21 and 1309.26(B).

²⁷ Ohio Rev. Code § 1309.21(D).

²⁸ Ohio Rev. Code § 1309.15.

²⁹ Ohio Rev. Code § 1309.26(A).

³⁰ Ohio Rev. Code § 1309.25.

It should also be remembered that a security agreement used in connection with a retail installment sale must include provisions complying with the Metzenbaum Act.³¹

Following is a sample security agreement covering consumer goods, equipment, and farm equipment. This form does not cover after acquired property or future advances and is not used in connection with a retail installment sale.

SECURITY AGREEMENT

_____19_____

(Name) (Street) (City) (County) (State)
(hereinafter called "Debtor") for valuable consideration, receipt whereof is hereby acknowledged, does hereby grant unto

(Name) (Street) (City) (County) (State)
(hereinafter called "Secured Party") a security interest in the property described below, together with any and all additions and accessions thereto (hereinafter called the collateral):
to secure the payment of _____ (\$) as provided in the note or notes of Debtor of even date herewith.

Warranties and Covenants of Debtor. Debtor hereby warrants and covenants that:

1. The collateral will be kept at _____
(Street) (City) (County)
_____. Debtor will notify Secured Party of any change in location
(State)
of the Collateral within Ohio and will not remove the Collateral from Ohio without the written consent of Secured Party. The Secured Party may examine and inspect the property at any time, wherever located.

2. The collateral is or is to be used primarily in _____
(insert one: (a) Personal, family or household purposes, (b) farming operations, (c) business use)

3. The collateral is (not) being acquired with the proceeds of the note or notes, which Secured Party may disburse directly to the seller of the collateral.

4. Debtor's place of business in this state is _____
(Street) (City)
_____ (if none, write "none") and all other places of business
(County)
of Debtor in this state outside of said county are located as follows:

5. If the collateral is used or bought primarily for personal, family or household purposes or for farming operations, or if Debtor has no place of business in this state, Debtor's residence is as above.

³¹ Ohio Rev. Code §§ 1317.01-1317.12 (1953).

6. If the collateral is of a type normally used in more than one state (such as automotive equipment, rolling stock, airplanes, road building equipment, commercial harvesting equipment, construction machinery and the like) Debtor's chief place of business is located at _____

7. If the collateral has been or is to be attached to real estate, the name of the record owner of such real estate is _____
_____ and said real estate is described as follows: _____

and if the Collateral is attached to real estate prior to the perfection of the security interest hereby granted, Debtor will upon demand furnish Secured Party with a disclaimer signed by all persons having an interest in the real estate, of any interest in the Collateral which is prior to Secured Party's interest.

8. Except for the security interest granted hereby, Debtor is the owner of the Collateral free from any prior lien, security interest or encumbrances, and Debtor will defend the Collateral against all claims and demands of all persons at any time claiming the same or any interest therein.

9. Debtor will not sell or offer to sell or otherwise transfer or encumber the property without written consent of Secured Party; will keep the collateral in good order and repair and will not waste or destroy the collateral.

10. No financing statement covering the collateral is on file in any public office, and at request of Secured Party, Debtor will join with Secured Party in executing one or more financing statements pursuant to the Uniform Commercial Code, as enacted in Ohio in form satisfactory to Secured Party and will pay the cost of filing the same in all public offices wherever filing is deemed necessary or desirable by Secured Party.

11. Debtor will keep the Collateral insured at all times against loss by fire and/or other hazards concerning which, in the judgment of the Secured Party, insurance protection is reasonably necessary, in a company or companies satisfactory to the Secured Party and in amounts sufficient to protect Secured Party against loss or damage to said Collateral; that such policy or policies of insurance will be delivered to the Secured Party, together with loss payable clauses in favor of the Secured Party as its interest may appear, in form satisfactory to the Secured Party.

Additional Rights of Parties. At its option, Secured Party may discharge taxes, liens, or security interests or other encumbrances at any time levied or placed on the Collateral, may pay for insurance on the Collateral and may pay for the maintenance and preservation of the Collateral. Debtor agrees to reimburse Secured Party on demand for any payment made, or any expense incurred by Secured Party pursuant to the foregoing authorization. Until default Debtor may have possession of the Collateral and use it in any lawful manner not inconsistent with this agreement and not inconsistent with any policy of insurance thereon.

Events of Default—Remedies. Upon the happening of any of the following events or conditions, namely: (a) default in the payment or performance of any of the obligations or of any covenant or liability contained or referred to herein or in any note evidencing any of the obligations; (b) any warranty, representation of statement made or furnished to Secured

Party by or on behalf of Debtor in connection with this agreement or to induce Secured Party to make a loan to Debtor proving to have been false in any material respect when made or furnished; (c) loss, theft, substantial damage, destruction, sale or encumbrance to or of any of the Collateral, or the making of any levy, seizure or attachment thereof or thereon; (d) death, dissolution, termination of existence, insolvency, business failure, appointment of a receiver of any part of the property of, assignment for the benefit of creditors by, or the commencement of any proceeding under any bankruptcy or insolvency laws by or against, Debtor or any guarantor or surety for Debtor; thereupon, or at any time thereafter (such default not having previously been cured) Secured Party at its option may declare all of the obligations to be immediately due and payable and shall then have the remedies of a secured party under the laws of the State of Ohio, including, without limitation thereto, the right to take possession of the Collateral, and for that purpose Secured Party may, so far as Debtor can give authority therefore, enter upon any premises on which the Collateral or any part thereof may be situated and remove the same therefrom. Secured Party may require Debtor to make the Collateral available to Secured Party at a place to be designated by Secured Party which is reasonably convenient to both parties. Secured Party will give Debtor at least five days' prior written notice of the time and place of any public sale thereof or of the time after which any private sale or any other intended disposition thereof is to be made, and at any such public or private sale Secured Party may purchase the collateral.

General. This agreement and the security interest in the Collateral created hereby shall terminate when the obligations have been paid in full. No waiver by Secured Party of any default shall be effective unless in writing nor operate as a waiver of any other default or of the same default on a future occasion. Secured Party is authorized to fill in any blank spaces herein and to date this agreement the date the loan is made. All rights of Secured Party hereunder shall inure to the benefit of the heirs, executors, administrators, successors and assigns of Secured Party; and all obligations of Debtor shall bind the heirs, executors, administrators, successors and assigns of Debtor. If there be more than one Debtor, their obligations hereunder shall be joint and several. This Agreement shall take effect when signed by Debtor.

IN WITNESS WHEREOF, Debtor has executed this agreement the

_____ day of _____, 19_____.

Debtor._____
Debtor._____

Secured Party_____

(To be signed by Secured Party only if
Agreement is to be filed)

COLLATERAL

Article 9 applies to goods, documents, instruments, general intangibles, chattel paper, accounts or contract rights, fixtures and any

sale of accounts, contract rights or chattel paper.³² The definitions of "account" and "contract right" are generally encompassed by the definition of "account receivable" under our existing Revised Code section 1325.01(A).

"General intangible," however, is a new term and is defined:

"General intangible" means any personal property, including things in action, other than goods, accounts, contract rights, chattel paper, documents, and instruments.

This term is intended more to cover new types of intangible collateral developed in the future than to cover any existing intangibles. However, the term could be applied to such things as good will and literary rights at the present time.

The term "document" is defined so as to include new types of documents which may develop and in other respects is in accord with existing Revised Code section 1315.01(F). "Chattel Paper," however, is a new term. It is a common practice for dealers in goods sold on an installment basis, to refinance the paper or instruments received. The term "chattel paper" is intended to cover not only the paper received but the interest of the dealer in the collateral covered thereby.

Goods are divided into four categories as set forth in Revised Code section 1309.07. This is probably the most important definition section contained in article 9. It states:

Goods are:

(A) "consumer goods" if they are used or bought for use primarily for personal, family, or household purposes;

(B) "equipment" if they are used or bought for use primarily in business, including farming or a profession, or by a debtor who is a non-profit organization or a governmental subdivision or agency or if the goods are not included in the definitions of inventory, farm products, or consumer goods;

(C) "farm products" if they are crops or livestock or supplies used or produced in farming operations or if they are products of crops or livestock in the unmanufactured states, such as ginned cotton, wool-clip, maple syrup, milk, and eggs, and if they are in the possession of a debtor engaged in raising, fattening, grazing, or other farming operations. If goods are farm products they are neither equipment nor inventory;

(D) "inventory" if they are held by a person who holds them for sale or lease or to be furnished under contracts of service or if he has so furnished them, or if they are raw materials, work in process, or materials used or consumed in a business. Inventory of a person is not to be classified as his equipment.

³² Ohio Rev. Code § 1309.02.

You will notice that the distinctions between these various categories depend upon the primary use of the property. Thus the same item of goods might fall into one or more categories. Take, for example, a television set. In the hands of the manufacturer or merchant it would be classified as inventory because it is held for sale. When used in a tavern or hotel, the same television set would be classified as equipment because it is used in a business. Bought for use in your home this television set would be classified as a consumer good. The question has been asked "What about the physician that uses a television set in his office waiting room but sometimes takes it home on weekends." You will notice that the test is the *primary* use, and in this case the primary use would seem to be in connection with the physician's profession. Thus the goods would be classified as "equipment."

It should be pointed out that, with respect to farm products, another test is added. The collateral must be in the hands of a debtor engaged in farming operations.³³

The definition of the term "instrument" contained in Revised Code section 1309.01(A)(7) is generally in accord with the definition of that term as it appears in our existing Revised Code section 1316.01(L). The new definition of instrument is:

"Instrument" means a negotiable instrument as defined in section 1303.03 of the Revised Code, or a security as defined in section 1308.01 of the Revised Code, or any other writing which evidences a right to the payment of money and is not itself a security agreement or lease and is of a type which is in ordinary course of business transferred by delivery with any necessary indorsement or assignment;

Proceeds are not defined as collateral subject to the provisions of Article 9. However, proceeds are defined to include:³⁴

Whatever is received when collateral or proceeds is sold, exchanged, collected, or otherwise disposed of. The term also includes the account arising when the right to payment is earned under a contract right. Money, checks, and the like are "cash proceeds." All other proceeds are "non cash proceeds."

The Code provides for a security interest in identifiable proceeds, including collections received by the debtor.³⁵

In the event of insolvency proceedings by or against the debtor a perfected security interest in proceeds covers identifiable cash and non-cash proceeds in the form of money, which have not been

³³ Ohio Rev. Code § 1309.07(C).

³⁴ Ohio Rev. Code § 1309.25(A).

³⁵ Ohio Rev. Code § 1309.25(A).

commingled or deposited, in a bank prior to the insolvency proceedings.³⁶ It also covers identifiable cash proceeds in the form of checks which have not been deposited.³⁷ If other cash proceeds have been commingled or deposited, such security interest covers all cash and bank accounts of the debtor, subject to any right of set off. In this event, the security interest is limited to the amount of cash proceeds received by the debtor within ten days before institution of the insolvency proceedings and deposited, less the amount of cash proceeds paid by the debtor to the secured party within such ten day period.³⁸

If the collateral covered by the perfected security interest has been sold and the interest has passed to the proceeds, a problem may be presented if the goods are returned to the debtor or repossessed by him. The security interest, as would be expected, attaches again to the goods when they are returned.³⁹ The problem arises out of the fact that the debtor may have transferred the account or chattel paper which arose from the sale of the goods to a second secured party for credit. Upon return of the goods there is a conflict between the transferee of the accounts or chattel paper and the secured party having the perfected security interest upon the goods. The Code establishes priorities between these parties.⁴⁰ These priorities may be stated:⁴¹

1. The inventory secured party takes priority over the transferee of the accounts receivable.

2. The transferee of the chattel paper who holds the same for new value and without knowledge of the existence of a security interest in the specific paper takes priority over the inventory secured party.

Accounts Receivable

When an account receivable has been given as security for an obligation or sold, the secured party takes subject to certain limitations as set forth in Revised Code section 1309.37 unless the account debtor has agreed not to assert defenses.

The secured party takes the account subject to the terms of the contract between the assignor and the account debtor and subject to any defense which the account debtor has against the assignor

³⁶ Ohio Rev. Code § 1309.25(D) (1) (2).

³⁷ Ohio Rev. Code § 1309.25(D) (3).

³⁸ Ohio Rev. Code § 1309.25(D) (4) (b).

³⁹ Ohio Rev. Code § 1309.25(E) (1).

⁴⁰ Ohio Rev. Code § 1309.25(E).

⁴¹ Ohio Rev. Code § 1309.25(E) (1) (2) (3) (4).

which accrues before notification that an assignment has occurred. The secured party is also bound by any good faith modifications of the contract between the assignor and the account debtor. Such modifications may be made without the secured party-assignee's consent. The secured party must notify the account debtor of the assignment or the account debtor is authorized to make payments to the assignor.

THE FLOATING LIEN

If you have heard the Uniform Commercial Code discussed, it is almost certain that you have heard the term "floating lien." Such term, however is not contained within the confines of the "Code." "Floating lien" is the phrase applied primarily to future advance and after acquired property provisions. The floating lien is a lien upon a moving stock of merchandise or inventory.

Such a lien is accomplished under the "Code" first by recognizing that inventory is intended for sale or incorporation into a product for ultimate sale. Thus Revised Code section 1309.26 authorizes a buyer in the ordinary course of business to take collateral free of a security interest created by his seller even though such interest is perfected and even though the buyer is aware of its existence. The second step is the reversal of case law, namely *Benedict v. Ratner*,⁴² which holds that unrestricted dominion or control of collateral by a debtor voids the lien of a secured party. Thus Revised Code section 1309.16 states:

A security interest is not invalid or fraudulent against creditors by reason of liberty in the debtor to use, commingle, or dispose of all or part of the collateral, including returned or repossessed goods, or to collect or compromise accounts, contract rights, or chattel paper, or to accept the return of goods, or make repossessions, or to use, commingle, or dispose of proceeds, or by reason of the failure of the secured party to require the debtor to account for proceeds or replace collateral.

Having assured the debtor's right to sell the collateral free of lien, the secured party must be given protection. He is given an automatic lien upon proceeds arising from such sale for a period of ten days.⁴³ If the financing statement filed covering the original collateral indicated that proceeds were also covered, this protection continues beyond the ten day period. If not, the secured party must perfect a security interest in the proceeds or his protection ceases at the end of the ten day period.⁴⁴

⁴² *Benedict v. Ratner*, 268 U.S. 353 (1925).

⁴³ Ohio Rev. Code § 1309.25(C).

⁴⁴ Ohio Rev. Code § 1309.25(C).

Inventory is constantly changing as sales are made and replacement inventory is received. The secured party is given additional protection as the Code authorizes a security agreement to provide that "collateral, whenever acquired shall secure all obligations covered by the security agreement."⁴⁵ To make this after acquired provision effective, the Code authorizes any description of the collateral if it reasonably identifies what is described.⁴⁶

A financing arrangement such as has been described is usually a continuing arrangement therefore "obligations covered by a security agreement may include future advances or other value whether or not the advances or value are given pursuant to commitment."⁴⁷

Objections have been raised to the floating lien on the ground that it will tend to create a monopoly of credit. This is a possibility but such does not seem to have happened in those states in which the Code is now effective. It can result in the debtor having no "free" assets with which to pay unsecured creditors in the event of insolvency proceeding. Proponents of the Code, however, advance the proposition that the businessman will better be able to finance himself under the Code and therefore less insolvencies will result. Only time will decide this issue.

PERFECTION OF THE SECURITY INTEREST

The steps required for attachment are constant. They do not vary according to type of collateral. Perfection, however, varies depending upon the type of collateral involved. Perfection may be accomplished by attachment alone, by possession or by filing. Discussion of these methods of perfection will be considered by class of collateral.

Goods

A security interest in goods may be perfected by filing or by possession; and a purchase money security interest in consumer goods, regardless of cost, and in farm equipment having an original purchase price not in excess of five hundred dollars, may be perfected simply by attachment.⁴⁸

Consumer Goods and Farm Equipment

The special rule which allows perfection of a purchase money security interest in consumer goods and farm equipment having an original purchase price of five hundred dollars or less without

⁴⁵ Ohio Rev. Code § 1309.15(C).

⁴⁶ Ohio Rev. Code § 1309.08.

⁴⁷ Ohio Rev. Code § 1309.15(C) (1962).

⁴⁸ Ohio Rev. Code § 1302.21(A)(3)(4).

possession or filing is entirely new in Ohio. The section stating that, in the case of such purchase money security interests, a purchaser for value without knowledge of the security interest who buys for his own personal, family or household purposes or farming operations takes free of the security interest is also new.⁴⁹ The two provisions taken together give pause for thought.

A prospective purchaser from the debtor who does not intend to use the collateral for personal or farming purposes or a prospective lender have no source of information as to whether or not the collateral is encumbered except the debtor. Yet, the security interest is enforceable against them even though not filed. Let us consider the following example: A. Rab purchases a piano from the RPC department store giving the seller a purchase money security interest for the entire purchase price. A week later A. Rab, needing funds, borrows two hundred dollars from the ROL-O finance company giving the piano as collateral. Assume RPC perfected its purchase money security by attachment without filing. Under the new Code ROL-O has no security for he did not purchase from the debtor for his own personal use or his own farming operations and RPC takes priority. A month later A. Rab sells his piano to A. Solo who wishes the piano for use in his recreation room. ROL-O perfected his security interest by filing. Filing was required for perfection even though the collateral was a consumer good because this was not a purchase money security interest. A. Solo owns the piano free of the claims of RPC but subject to the security interest of ROL-O who has filed. The provisions discussed can cause problems.

Inventory

Attention should also be called to special provisions surrounding the perfection of a purchase money security interest in inventory. When a security interest covering after acquired property has been perfected in inventory, persons selling replacement inventory to the debtor may wish to obtain a purchase money security interest in the merchandise they supply. To perfect a purchase money security interest in inventory such interest must be perfected prior to delivery of the collateral to the debtor. The secured party having the existing security interest must be given notice of the purchase money security interest before possession of the goods covered thereby is given to the debtor.⁵⁰ The notice must contain a description of the goods by item or type and a statement that the person giving the notice has or expects to have a purchase money security interest in inventory of

⁴⁹ Ohio Rev. Code § 1309.26(B).

⁵⁰ Ohio Rev. Code § 1309.31(C).

the debtor.⁵¹ If these steps are not taken, an existing perfected security interest will take priority.

Possession

Perfection of a security interest in goods by possession is also subject to special treatment under the Code. The secured party may have actual possession of the goods or they may be in the actual physical possession of a bailee. If the goods are in the physical possession of a bailee who has not issued a negotiable document therefor, such possession is regarded as possession by the secured party from the time the bailee is notified of his interest.⁵²

If the goods are in the possession of the issuer of a negotiable document therefor, a security interest in the goods may only be effectively perfected by perfecting a security interest in the document. A security interest in the goods perfected in any other way is subject to the security interest in the document.⁵³ Perfection by possession does not relate back, it dates only from the time possession is taken.⁵⁴ However, goods may be released temporarily to the debtor for a limited purpose, including sale, and the security interest continues perfected.⁵⁵ Temporary release is limited to twenty-one days.⁵⁶ A similar provision for return of goods for temporary use is found in our factor's lien act.⁵⁷

Accounts, Contract Rights, and General Intangibles

Security interest in accounts, contract rights, and general intangibles is perfected only by filing. There is nothing which may be taken into possession.

Instruments, Documents, and Chattel Paper

A security interest in instruments may be perfected only by possession. However, a security interest in a negotiable instrument is perfected by attachment only, for a period of twenty-one days to the extent that the security interest arises for new value given under a written security agreement.⁵⁸

Perfection of a security interest in documents or chattel paper may be accomplished by possession or filing. However, a security

⁵¹ Ohio Rev. Code § 1309.31(C)(3).

⁵² Ohio Rev. Code § 1309.24.

⁵³ Ohio Rev. Code § 1309.23(B).

⁵⁴ Ohio Rev. Code § 1309.24.

⁵⁵ Ohio Rev. Code § 1309.23(E)(1).

⁵⁶ Ohio Rev. Code § 1309.23(E)(1).

⁵⁷ Ohio Rev. Code § 1311.60.

⁵⁸ Ohio Rev. Code § 1309.23(E).

interest in a negotiable document is perfected by attachment only, for a period of twenty-one days to the extent that the security interest arises for new value given under a written security agreement.⁵⁹

A security interest in a document continues perfected even though the document is released to the debtor so as to enable him to deal with the goods represented thereby for a limited purpose. Such temporary perfection continues for only twenty-one days.

A holder in due course of a negotiable instrument or a holder to whom a negotiable document of title has been duly negotiated take priority over an earlier perfected security interest.⁶⁰

A purchaser of chattel paper or a non-negotiable instrument for new value who takes possession of such collateral in the ordinary course of his business, without knowledge that the paper or instrument is subject to a security interest takes priority.⁶¹

Because of the priorities of holders and good faith transferees stated, one must conclude that the only practical way to perfect a security interest in instruments, documents or chattel paper is by possession.

Filing

When perfection is to be accomplished by filing, the Code provides that a "financing statement" must be filed. The security agreement may be filed in lieu of the financing statement if the security agreement meets the formal requirements of a financing statement. These requirements are that it be signed by the debtor and the secured party, give an address for both and contain a statement indicating the types or describing the items of collateral. "When the financing statement covers crops growing or to be grown or goods which are or are to become fixtures, the statement must also contain a description of the real estate concerned."⁶² If a security interest is desired in proceeds for longer than the automatic ten day period, the financing statement must so reflect.

The provisions of Revised Code section 1309.08 making any description which reasonably identifies the collateral sufficient also applies to the financing statement.

⁵⁹ Ohio Rev. Code § 1309.23(E).

⁶⁰ Ohio Rev. Code § 1309.28.

⁶¹ Ohio Rev. Code § 1309.27.

⁶² Ohio Rev. Code § 1309.14(A)(2).

The following is a form of financing statement:

This Financing Statement is presented to a filing officer for filing pursuant to the Uniform Commercial Code. Maturity date (if any)

1. Debtor(s) (Last Name First) and address(es)	2. Secured Party(ies) and address(es)	3. For Filing Officer (Date, Time, Number, and filing office)
---	--	--

4. This financing statement covers the following types (or items of property):

Check X if covered	Proceeds of Collateral are also covered	Products of Collateral are also covered	Number of additional sheets presented:
--------------------------	--	--	---

Filed with

By _____
Signature(s) of Debtor(s)

By _____
Signature(s) of Secured Party(ies)

The form of filing prescribed under Article 9 is termed "notice filing." This form may be contrasted with "record filing." The difference between the two lies in the amount of information contained in instruments filed and the purposes of the filing. Notice filing is intended simply to advise the public that an arrangement exists, not necessarily the details. The financing statement is filed to put interested persons on notice that a financing arrangement exists between the debtor and the secured party who claims an interest in the collateral described.

Contrast this, for example, with record filing under our chattel mortgage statutes.⁶³ The instrument itself is recorded, theoretically setting forth the entire transaction. The amount of the obligation is shown and a detailed description of the collateral is given. At any given moment, the actual obligation cannot be determined from this "record." Only the original amount of the obligation is shown.

Notice filing is not new, however, to Ohio. This is the form of filing required under our present trust receipt,⁶⁴ factor's lien,⁶⁵ and assignment of accounts receivable⁶⁶ acts.

Many objections have been raised to this form of filing in connection with the adoption of article 9. Under the liberal description requirements of the Code together with Code provisions relating to

⁶³ Ohio Rev. Code § 1319.02 (1953).

⁶⁴ Ohio Rev. Code § 1316.24 (1953).

⁶⁵ Ohio Rev. Code § 1311.61 (1953).

⁶⁶ Ohio Rev. Code § 1325.03.

after acquired property and future advances it has been felt that it would be impossible to determine the specific collateral or obligation covered from public records. This would seem to be true.

The purpose of notice filing being simply to advise of the arrangement, provision was made for the debtor to obtain a statement from the secured party as to the collateral covered by the security interest and the amount of the obligation due at any time. A prospective lender or purchaser may obtain this same information by demanding that the debtor present such a statement as a condition of purchase or granting the loan sought. Specifically the Code provides that the debtor may send his signed statement "indicating what he believes to be the aggregate amount of unpaid indebtedness as of a specified date"⁶⁷ to the secured party with a request that the statement be approved or corrected and returned. He may also request the secured party to approve or correct a list of the collateral if records of the secured party identify the same.⁶⁸

The secured party is given two weeks within which to comply and if he fails to do so he is liable for any loss caused to the debtor thereby. If the request included a statement as to collateral, the secured party may claim a security interest only in the collateral as shown in such statement, "against persons misled by his failure to comply."⁶⁹ A debtor is entitled to one such statement every six months without charge. The debtor may charge not in excess of ten dollars for each additional statement.⁷⁰

Place of Filing

Filing may be local only, central only or a combination of both. The last is sometimes called, "dual filing." Ohio has adopted dual filing. In Ohio, after July 1, 1962, if central filing is required it is to be made with the Secretary of State. If local or county filing is required, filing is with the county recorder.

Transactions considered essentially local, require county filing. Thus, when the collateral is equipment used in farming operation, or accounts, contract rights or general intangibles arising from or relating to the sale of farm products by a farmer, or consumer goods, filing is in the county of the debtors residence or, if a non-resident, in the county where the goods are located, and in addition, if the collateral is crops, filing is in the county where the real estate is located. If the

⁶⁷ Ohio Rev. Code § 1309.19(A).

⁶⁸ Ohio Rev. Code § 1309.19(A).

⁶⁹ Ohio Rev. Code § 1309.19(B).

⁷⁰ Ohio Rev. Code § 1309.19(C).

collateral is or is to become a fixture, filing is also in the county where the real estate is located.⁷¹

In all other cases, filing is with the Secretary of State and, in addition, if the debtor has a place of business in only one county in Ohio, also in the county where that place of business is located. If the debtor has no place of business in this state but resides here, filing is also in the county of his residence.⁷²

Effect of Failure to File

A filing which is not made in all required places or in an improper place is effective against any person who has actual knowledge of the contents of the financing statement. Thus, the person who has seen the financing statement could not effectively raise the defense that such financing statement is filed in the wrong place.⁷³ This is a decided change from present law.

A filing made in an improper place or not made in all places required is nevertheless effective with regard to any collateral for which the filing was proper.⁷⁴ A financing statement might cover consumer goods and business equipment of a resident debtor having a place of business in only one county in Ohio. Under these circumstances filing with the county recorder of the county in which the debtor's place of business is located would be required as to the equipment. If filing was had only in the county in which the debtor resided, the filed financing statement would not be effective as to the equipment but would be effective as to the consumer goods.

Duration, Termination, Release, Continuation, and Assignment

A filed financing statement is effective for five years, unless such statement shows a maturity date of the obligation as being five years or less in which case the filing is effective until such maturity date and for sixty days thereafter.⁷⁵

A continuation statement may be filed within six months before and sixty days after a stated maturity date of five years or less and, when no maturity date is stated, within six months prior to the expiration of the five year period.⁷⁶ If no continuation statement is filed within such time limitations, the filing lapses and the security interest becomes unperfected. A continuation statement extends the original filing for a period of five years.

⁷¹ Ohio Rev. Code § 1309.38(A)(2).

⁷² Ohio Rev. Code § 1309.38(A)(3).

⁷³ Ohio Rev. Code § 1309.38(A).

⁷⁴ Ohio Rev. Code § 1309.38(B).

⁷⁵ Ohio Rev. Code § 1309.40(B).

⁷⁶ Ohio Rev. Code § 1309.40(C).

A continuation statement need only be signed by the secured party, identify the original instrument filed by file number, and state that the same is still effective.⁷⁷

A secured party may release all or any part of collateral covered by a filed financing statement by filing his signed statement describing the collateral to be released, setting forth the names and addresses of the parties and identifying the financing statement by file number.⁷⁸

Assignment of a security interest may be accomplished by filing a separate instrument showing the names and addresses of the secured party, debtor, and assignee, and identifying the collateral⁷⁹ and the financing statement by file number. A copy of the assignment itself may be filed if it meets the stated requirements. When a separate instrument is filed it must be signed by the secured party.⁸⁰

Assignment may also be accomplished by notation on the financing statement of the name and address of the assignee or of an assignment itself.⁸¹

The debtor may make written demand upon the secured party for a termination statement when the obligation has been extinguished and there are no commitments to make advances. If the secured party fails to send such a termination statement to the debtor within ten days after the demand, he becomes liable to the debtor for the sum of one hundred dollars and any resulting loss to the debtor.⁸²

Fixtures, Accessions, and Commingled Goods

The new statutes do not define either a fixture or an accession. The law of Ohio as to what is a fixture or accession remains unchanged. The Code does state that the rules laid down for fixtures do not apply to "goods incorporated into a structure in the manner of lumber, bricks, tile, cement, glass, metal work and the like. . . ." ⁸³ Rather, the Code is concerned with conflicts of interest between the holder of a security interest in the fixture and the holder of an interest in the real estate or personal property to which the collateral has been attached.

A security interest attached to goods before they become fixtures takes priority over the claims of all persons having an interest in the real estate.

A security interest attaching to goods after they become fixtures

⁷⁷ Ohio Rev. Code § 1309.40(C).

⁷⁸ Ohio Rev. Code § 1309.43.

⁷⁹ Ohio Rev. Code § 1309.42(A).

⁸⁰ Ohio Rev. Code § 1309.42(B).

⁸¹ Ohio Rev. Code § 1309.42(A).

⁸² Ohio Rev. Code § 1309.41.

⁸³ Ohio Rev. Code § 1309.32.

is effective against persons subsequently acquiring interests in the real estate. Both the "before" and "after" rule are subject to the exception in section 1309.33(D) that these interests do not take priority over:

(1) a subsequent purchaser for value of any interest in the real estate; or

(2) a creditor with a lien on the real estate subsequently obtained by judicial proceedings; or

(3) a creditor with a prior encumbrance of record on the real estate to the extent that he makes subsequent advances; if the subsequent purchase is made, the lien by judicial proceedings is obtained, or the subsequent advance under the prior encumbrance is made or contracted for without knowledge of the security interest and before it is perfected. A purchaser of the real estate at a foreclosure sale other than an encumbrancer purchasing at his own foreclosure sale is a subsequent purchaser within this section.

A security interest which attaches after the goods have become fixtures is invalid against persons with an interest in real estate at the time the security interest attaches who have not given written consent to the security interest or disclaimed any interest in the goods as fixtures.

Upon default, a secured party having priority over the claims of all persons having an interest in the real estate may remove his collateral from the real estate but must reimburse an encumbrancer or owner of the real estate for the cost of repairs for any damage done in such removal. Loss in value of the real estate by reason of the absence of the collateral may not be recovered.

The rules relating to accessions are identical with those for fixtures.

Commingled Goods

If goods upon which there is a perfected security interest are commingled and become part of a product or mass so that they are no longer identifiable, the security interest continues in the mass or product.⁸⁴ The security interest also continues in the product or mass if the financing statement covering the original goods also covered products of the collateral.⁸⁵

When more than one security interest attaches to the mass, the value of each is determined according to the ratio of the cost of the goods to which each interest originally attached bears to the cost of the total product or mass.

⁸⁴ Ohio Rev. Code § 1309.34.

⁸⁵ Ohio Rev. Code § 1309.34(A)(2).

PRIORITIES

Special rules of priority relating to instruments, documents, chattel paper, proceeds, fixtures, and purchase money security interests in inventory have been discussed.

The general rules of priority are:⁸⁶

1. The priority as between unperfected security interests in the same collateral is determined according to the order of attachment.

2. A perfected security interest takes priority over an unperfected security interest.

3. The priority of perfected security interests in the same collateral is:

(a) "in the order of filing if both are perfected by filing"⁸⁷ and

(b) "in the order of perfection unless both are perfected by filing."⁸⁸

4. "A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter."⁸⁹

Under the rules stated, if A and B both had security interests in the same desk and both had filed financing statements to perfect their interest, the financing statement bearing the earlier filing date would take priority.

On the other hand, let us assume that A perfects his security interest on January 1 by taking possession of the desk, and B perfects his interest by filing on January 10. A would take priority as both security interests were not perfected by filing, and the first to perfect rule applies.

An interesting situation is presented by future advances and the rules of priority under the Code. Let us assume that A loans B \$5,000.00 on January 1, provides for future advances in his security agreement, and files his financing statement on the same date. On February 1, C loans B \$5,000.00 and perfects his security interest by filing on that date. Both security interests cover the same collateral. On March 1, A loans B an additional \$5,000.00 under the future advance provision in their agreement. A has priority in the collateral to the extent of \$10,000.00 which comes before B, even though the second loan by A was subsequent to the time B per-

⁸⁶ Ohio Rev. Code § 1309.31.

⁸⁷ Ohio Rev. Code § 1309.31(E)(1).

⁸⁸ Ohio Rev. Code § 1309.31(E)(2).

⁸⁹ Ohio Rev. Code § 1309.31(D).

fects his security interest. This results because the future advance by A relates back to the date of perfection of his security interest, to wit, January 1.

Special Rules

Unperfected security interests are subordinate to the claims of lien creditors who become such without knowledge of the security interest and before it is perfected.⁹⁰ A lien creditor is defined as:

A "lien creditor" means a creditor who has acquired a lien on the property involved by attachment, levy or the like and includes an assignee for benefit of creditors from the time of assignment, and a trustee in bankruptcy from the date of the filing of the petition or a receiver in equity from the time of appointment. Unless all the creditors represented had knowledge of the security interest such a representative of creditors is a lien creditor without knowledge even though he personally has knowledge of the security interest.⁹¹

Unperfected liens are also subordinate to the rights of:

In the case of goods, instruments, documents, and chattel paper, a person who is not a secured party and who is a transferee in bulk or other buyer not in ordinary course of business to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected.

In the case of accounts, contract rights, and general intangibles, a person who is not a secured party and who is a transferee to the extent that he gives value without knowledge of the security interest and before it is perfected.⁹²

Perfected security interests are also subject to liens given by statute or rule of law to a person who furnishes services or materials with respect to the collateral subject to a security interest.⁹³

RIGHTS AND DUTIES OF SECURED PARTY

When the secured party is in possession of the collateral, he must use reasonable care to preserve the same which, in the case of chattel paper or an instrument, includes taking steps to preserve rights against prior parties.⁹⁴ Presentment would be such a step.

The secured party "must keep the collateral identifiable but fungible collateral may be commingled."⁹⁵ He may pledge the col-

⁹⁰ Ohio Rev. Code § 1309.20.

⁹¹ Ohio Rev. Code § 1309.20(C).

⁹² Ohio Rev. Code § 1309.20(A)(3)(4).

⁹³ Ohio Rev. Code § 1309.29.

⁹⁴ Ohio Rev. Code § 1309.18.

⁹⁵ Ohio Rev. Code § 1309.18(B)(1).

lateral and may hold any increase or profits as additional security except money which must be applied on the obligation.

Risk of loss is upon the debtor and reasonable expenses of preservation of the collateral, such as insurance, are chargeable to the debtor.⁹⁶

DEFAULT

Rights of Collection

A secured party may notify and collect from an account debtor and take control of any proceeds to which he is entitled upon default.⁹⁷

A secured party, entitled to charge back or otherwise to recourse against the debtor by agreement, who proceeds to collect from account debtors must do so in a reasonably commercial manner. If the security arrangement was one of indebtedness, the secured party must account for any surplus and the debtor is liable for any deficiency. On the other hand, if the arrangement was a sale of accounts, contract rights or chattel paper, the debtor is neither liable for a deficiency nor entitled to any surplus unless the agreement so provides.⁹⁸

Repossession

If repossession can be accomplished without breach of the peace, the secured party may do so, otherwise it must be done by judicial process. If the agreement so provides a secured party may require the debtor to assemble the collateral and make it available at a place designated by the debtor. A secured party may render equipment unusable.⁹⁹ This is a new authorization under Ohio law.

Disposal Of Collateral

A secured party may retain the collateral in complete satisfaction of the debt if he receives no objection within thirty days after notifying the debtor and, except in the case of consumer goods, any other person having a security interest in the collateral who has filed or is known to the secured party.¹⁰⁰ The secured party may not retain the collateral if the same is consumer goods and the debtor has paid sixty per cent of the loan or purchase price, if purchased on installments. Under present law the secured party need not dispose of the collateral covered by a chattel mortgage unless he desires to collect a deficiency.¹⁰¹

⁹⁶ Ohio Rev. Code § 1309.18.

⁹⁷ Ohio Rev. Code § 1309.45(B).

⁹⁸ Ohio Rev. Code § 1309.45(B).

⁹⁹ Ohio Rev. Code § 1309.46.

¹⁰⁰ Ohio Rev. Code § 1309.48.

¹⁰¹ Ohio Rev. Code § 1319.07 (1953).

When disposal of the collateral is desired or required, the secured party may sell, lease or "otherwise dispose"¹⁰² of the collateral. Disposition may be by public or private proceedings.¹⁰³ Unless the collateral is perishable or threatens to decline in value rapidly, the secured party must give reasonable notice of the time and place of any public sale or after which any private sale will be made.¹⁰⁴ Such notice must be sent to the debtor and, except when the collateral is consumer goods, to any other person having a security interest in the collateral, who has filed a financing statement in this state or is known to the debtor.¹⁰⁵ Present statutes require that ten day notice be given.¹⁰⁶

Any surplus upon disposition is to be accounted for to the debtor and he is liable for any deficiency. Where the transaction was one of sale of accounts, contract rights or chattel paper the debtor is neither entitled to any surplus or liable for any deficiency unless the agreement so provides.¹⁰⁷

Proceeds of Any Disposition

Funds coming into the hands of the secured party as a result of sale of repossessed goods must be applied in the following order:¹⁰⁸

1. The reasonable expenses of retaking, holding, preparing for sale, selling, and the like.

2. The satisfaction of indebtedness secured by the security interest under which the disposition is made.

3. The satisfaction of indebtedness secured by any subordinate security interest in the collateral if written notification of demand therefor is received before distribution of the proceeds is completed. If requested by the secured party, the holder of a subordinate security interest must seasonably furnish reasonable proof of his interest, and unless he does so, the secured party need not comply with his demand.

Debtor's Right of Redemption

At any time before the secured party has disposed of or contracted to dispose of the collateral, after repossession, the debtor may redeem the collateral. A prerequisite of such redemption is tender of the full amount of the obligations and expenses of retaking incurred by the secured party.¹⁰⁹ It is also to be noted that this right of redemption

¹⁰² Ohio Rev. Code § 1309.47(A).

¹⁰³ Ohio Rev. Code § 1309.47(C).

¹⁰⁴ Ohio Rev. Code § 1309.47(C).

¹⁰⁵ Ohio Rev. Code § 1309.47(C).

¹⁰⁶ Ohio Rev. Code § 1319.07.

¹⁰⁷ Ohio Rev. Code § 1309.47(B).

¹⁰⁸ Ohio Rev. Code § 1309.47(A).

¹⁰⁹ Ohio Rev. Code § 1309.49.

is granted to any other secured party who claims an interest in the collateral.

CONCLUSION

To discuss Article 9 of the Uniform Commercial Code adequately would require much more space than is here allotted. It is hoped that the material set forth in this article will create an awareness that many changes are in store for the lawyers of Ohio and serve as an outline of the act itself. The steps set forth to perfect a security interest are simple if the lawyer will remember the classifications of collateral and the places of filing. The ramifications of "notice filing," the "floating lien," and non-filing on consumer goods will be determined only in the light of experience.